

**MOUNTAIN REGIONAL WATER
SPECIAL SERVICE DISTRICT
A COMPONENT UNIT OF SUMMIT COUNTY, UTAH**

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**To The Audit Committee of the Summit County Commission
Mountain Regional Water Special Service District**

Independent Auditors' Report

We have audited the accompanying basic financial statements of Mountain Regional Water Special Service District (the District), a component unit of Summit County, Utah, as of and for the years ended December 31, 2005 and 2004, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Mountain Regional Water Special Service District as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 28, 2006, on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Schmitt, Giffels, Smith & Co., P.C.

April 28, 2006

Management's Discussion and Analysis

**Mountain Regional Water
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This section of the Mountain Regional Water Special Service District of Summit County (District) report presents management's discussion and analysis of the District's financial performance during the year ended December 31, 2005. Please read it in conjunction with the District's basic financial statements, which follow this section.

Financial Highlights

In 2005, the District's financial condition improved significantly for the third straight year as an accelerating building boom resulted in continued strong growth in lot sales and building activity that greatly exceeded projections. As a point of caution, with a fixed level of future development potential within the District's boundaries, this strong growth and the related high level of connection fee, impact fee, and special assessment collections cannot continue indefinitely.

The extra impact fees and special assessments collected during the building boom are required by both state law and bond covenants to be set aside for future debt service payments. As such, when the building boom subsides, sufficient funds will be available to continue to make debt service payments for several years without creating an additional burden on District rate payers. The District will evaluate the benefits of paying debt off early once the opportunity exists.

Net Income

The District's 2005 net income of \$5.5 million was driven by four main factors:

1. Promontory Special Improvement District (SID) assessment collections totaled nearly \$5.2 million. After the related interest income and interest expense is taken into account, this SID accounted for nearly \$4.5 million, or 81.5% of net income.

An SID assessment is charged to the Promontory developer each time it sells a lot within the SID, and then set aside to make future debt payments on the corresponding \$18.6 million SID bond. The SID includes 1,500 total lots. In future years, the net income related to the Promontory SID could be negative because the early lots sales and related assessment collections have far exceeded expectations, meaning future collections will be less. Long-term, the total net cash flow for the Promontory SID will be zero.

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Current excess collections have been set aside in a restricted escrow account for future debt payments. Legally and contractually, the SID collections may not be used for any other purpose. The District will analyze the benefits of prepaying a portion of the SID bond principal in 2008 – which is as soon as allowed by the bond covenants. In 2005, the District collected special assessments for 278 Promontory lots. The District needs to collect roughly 100 SID assessments each year to fund the related principal payments. Because lot sales in Promontory have been much higher than projected, the District currently has \$3.5 million in excess funds in the bond fund and \$3.1 million in the debt service fund for a total of \$6.6 million.

It is important to note that interest payments on the Promontory SID bonds must be paid solely by Promontory developers. The developers must also cover any shortfall in principal assessments. Thus, the District has no legal requirement to pay off any related debt service for the Promontory bonds other than from SID assessments. The undeveloped land in the Promontory development provides the full collateral for the bond holders.

2. Because of regulatory delays on the Lost Canyon water importation project, which is now complete, depreciation expense was \$185,843 less than budgeted for 2005 while interest expense was \$411,176 under budget.

Although interest expense was below budget, the amount budgeted was paid to bond holders in 2005 as scheduled. \$383,603 of the District's interest payments were capitalized - or in more laymen terms - included as part of the construction costs for the capital projects funded by the related debt. Accounting standards require interest expense to be capitalized until the projects funded by the related debt proceeds are complete. Further, capital infrastructure costs are not expensed when constructed or acquired; they are expensed as depreciation in future years over their useful life. In addition, \$21,811 of interest expense was either accrued or amortized.

Since the completion of the Lost Canyon project was delayed until early 2005 due to regulatory issues, it was depreciated over fewer months in 2005 than initially anticipated, causing 2005 depreciation expense to be \$183,843 under budget.

3. Connection fees related to the building boom exceeded budget by \$317,745. This is one-time revenue that will subside once the building boom slows. Thus, the extra funds will be used in 2006 to acquire much needed capital equipment and to replace old vehicles, and not to increase ongoing expenditures.
4. Water sales exceed projections by \$402,394 in 2005. This increase is mostly due to the rapid growth of the Promontory and Glenwild resort developments. Because of accelerating lot sales, the Promontory developer started its second golf course two years ahead of schedule and utilized large quantities of construction water for the development of new residential plats. Promontory also started the design of its third golf course several years ahead of schedule due to the high lot sales.

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The District added 243 water users within its current boundaries in 2005, an increase of 10.4%, while Promontory platted an additional 453 lots for which standby fees will be collected until a home is completed on a lot. In addition, the District implemented accelerated conservation rates in 2005 that increase the water usage charges for customers using large amounts of water. These conservation rates were recommended by a committee of District customers.

Because of strong growth in water sales, which is ongoing revenue, the District reduced the standby fee from \$38.50 to \$33.50 in January 2006. In May 2006, the District reduced the rate charged to condominium homeowner's associations for water used to water each unit's front and back yards in order to make this rate more comparable to an equal number of residential water users consuming outdoor water. The lower rate does not apply to amenities provided by condominium homeowner's associations such as lakes, waterfalls, parks, trails, swimming pools, common space, etc.

The District's net income is shown below by three categories:

Mountain Regional Water Special Service District's Income Statement Components

	<u>Total 2005</u>	<u>Operations 2005</u>	<u>Promontory SID 2005</u>	<u>Project Funds 2005</u>
Operating revenues:				
Water sales	\$ 4,052,394	\$ 4,052,394	\$ -	\$ -
Connection fees	483,745	483,745	-	-
Service	10,479	10,479	-	-
Other	188,743	188,743	-	-
Total operating revenue	<u>4,735,361</u>	<u>4,735,361</u>	<u>-</u>	<u>-</u>
Operating Expenses:				
Water production	747,972	747,972	-	-
Engineering and water development	94,037	94,037	-	-
Operations, maintenance and repairs	1,069,234	1,069,234	-	-
Management and finance	284,423	284,423	-	-
Legal services	86,019	86,019	-	-
Depreciation	1,053,157	1,053,157	-	-
Total operating expenses	<u>3,334,842</u>	<u>3,334,842</u>	<u>-</u>	<u>-</u>
Operating income	<u>1,400,519</u>	<u>1,400,519</u>	<u>-</u>	<u>-</u>
Non-operating revenues (expenses)				
State grants	11,667	11,667	-	-
Interest income	457,382	242,634	171,157	43,591
Impact fees	704,709	704,709	-	-
SID assessments	5,182,900	-	5,182,900	-
Gain on sale of fixed assets	169,846	-	-	169,846
Other non-operating revenue	115,896	-	-	115,896
Interest expense	(2,399,724)	(1,597,143)	(802,581)	-
Trustee and bank fees	(35,664)	(29,664)	(6,000)	-
Bond issuance cost amortization	(107,882)	(45,112)	(62,770)	-
Total non-operating revenues (expenses)	<u>4,099,130</u>	<u>(712,910)</u>	<u>4,482,707</u>	<u>329,333</u>
Income before operating transfers	<u>\$ 5,499,649</u>	<u>\$ 687,609</u>	<u>\$ 4,482,707</u>	<u>\$ 329,333</u>

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New Infrastructure

The District's massive capital projects initiative to address the water shortage and quality problems within its service areas is now complete. This includes the Lost Canyon pipeline and Signal Hill treatment plant, the first major importation project to bring much needed water into the Snyderville Basin of Summit County. In 2004, the District began pumping irrigation water from the Rockport area on the east side of Summit County through new wells, booster pumps and a pipeline to water the first Promontory golf course. The Signal Hill Treatment Plant is now operational and provides culinary water to both Promontory and other service areas within the District.

Another critical project was completed in early 2005 that increased the District's pipeline capacity underneath US Highway 40 in the Atkinson service area. This project allows more water from the Justice Center Well on the east side of the highway to be transported to the west side of the highway within the Atkinson service area. In addition, it allows more water from the Lost Canyon water importation project to be transported to all other service areas within the District.

Overview of Basic Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. These statements comprise two components: 1) its enterprise fund financial statements, and 2) notes to the basic financial statements. These statements include all District activities.

Component Unit Financial Statements

The District operates as an enterprise fund and is a component unit of Summit County, Utah. Enterprise funds account for operations that are financed and operated in a manner similar to a private business enterprise where the intent of the governing body is that the costs of providing goods and services to the general public be financed or recovered primarily through user charges. The District is financed primarily through water sales, service fees, and impact fees. The District does not impose any taxes.

Notes to Financial Statements

The notes provide additional information essential to a full understanding of the data provided in the financial statements. The notes are a part of the basic financial statements.

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District Financial Analysis

Net Assets

An entity's net asset position may serve over time as a useful indicator of a government's financial position. As shown below, overall net assets increased nearly \$5.5 million or 90.0% in 2005 from net income. Between 2003 and 2004 net assets increased over \$2.5 million or 72.1% from net income as well. This demonstrates strengthened financial condition for the former financially struggling water companies acquired or annexed by the District.

Mountain Regional Water Special Service District's Change in Net Assets

				\$	%
	2005	2004	2003	Change 2005 to 2004	Change 2005 to 2004
Operating revenue	\$ 4,735,361	\$ 3,633,680	\$ 2,621,017	\$ 1,101,681	30.3 %
Operating expenses	(3,334,842)	(2,777,177)	(2,780,693)	(557,665)	20.1
Operating income (loss)	1,400,519	856,503	(159,676)	544,016	63.5
Non-operating revenue	6,642,400	4,265,920	2,483,221	2,376,480	55.7
Non-operating expense	(2,543,270)	(2,563,077)	(1,956,107)	19,807	(0.8)
Income before operating transfers	5,499,649	2,559,346	367,438	2,940,303	114.9
Transfers and contributions to (from) district	-	-	(387,337)	-	-
Change in net assets	5,499,649	2,559,346	(19,899)	2,940,303	114.9
Net assets - beginning	6,111,060	3,551,714	3,571,613	2,559,346	72.1
Net assets - ending	\$ 11,610,709	\$ 6,111,060	\$ 3,551,714	\$ 5,499,649	90.0 %

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The District's net assets can be segregated into three categories to provide more insight into its financial condition, as shown below.

Mountain Regional Water Special Service District's Net Assets

				\$	%
	2005	2004	2003	Change 2005 to 2004	Change 2005 to 2004
Unrestricted current assets	\$ 1,945,361	\$ 1,299,435	\$ 1,330,064	\$ 645,926	49.7 %
Capital assets	47,999,746	47,381,134	35,437,081	618,612	1.3
Other assets	14,576,900	12,133,421	54,696,909	2,443,479	20.1
Total assets	64,522,007	60,813,990	91,464,054	3,708,017	6.1
Current liabilities	678,270	872,256	1,179,900	(193,986)	(22.2)
Long-term liabilities	50,512,758	52,066,073	52,655,473	(1,553,315)	(3.0)
Other liabilities	1,720,270	1,764,601	34,076,967	(44,331)	(2.5)
Total liabilities	52,911,298	54,702,930	87,912,340	(1,791,632)	
Net assets					
Invested in capital assets, net of related debt	7,198,771	3,631,451	2,109,000	3,567,320	98.2
Restricted	1,802,768	859,252	2,028,002	943,516	109.8
Unrestricted	2,609,170	1,620,357	(585,288)	988,813	61.0
Total net assets	\$ 11,610,709	\$ 6,111,060	\$ 3,551,714	\$ 5,499,649	90.0 %

Net assets invested in capital assets, net of related debt is calculated simply by taking fixed assets (less depreciation) plus restricted cash for debt service and the remaining bond proceeds minus the outstanding principal due on the debt used to fund those assets. The increases for 2004 and 2005 are largely the result of principal payments made during the year on related debt, and an increase in the debt service fund balances from SID assessment collections.

Restricted net assets includes other restricted cash accounts less liabilities that will be paid exclusively from future restricted revenue collections, particularly future impact fees collected from The Colony service area. The developer prepaid most impact fees for The Colony service area and will be reimbursed by the District as it collects the impact fee from lot owners when the developer sells a lot.

Restricted net assets increased in 2005 because the District set aside \$285,742 collected from the sale of surplus land and a one-time payment from a developer for future construction projects, and because the District deposited a portion of its revenue collections in reserve accounts. Restricted net assets declined between 2003 and 2004 as funds set aside for construction projects that were not obtained through borrowing were spent on infrastructure and other assets.

Unrestricted net assets increased in both 2004 and 2005 due to positive operating income and because restricted funds were used to construct unrestricted assets. Unrestricted net assets improved to just over \$2.6 million in 2005 after being in a deficit position until 2004.

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Summary of Revenues

As shown below, the District experienced a 30.3% increase in operating revenue between 2004 and 2005. This resulted from several factors. First, the District implemented conservation based water usage charges for high users in hopes of promoting conservation. Although the District did see a reduction of water use for some of these customers, it was not as much as expected. In addition, the District experienced 10.4% growth in new customers using water as 243 new homes connected to the system in 2005. Nearly 500 new lots were platted generating additional standby fees (a charge assessed on vacant lots until they are developed). The continued building boom resulted in increased connection fees in 2005 as well, although this level of connection fee revenue is not sustainable in the long run. Operating revenue increased in 2004 due to a rate increase and customer growth as well.

Mountain Regional Water Special Service District's Revenue Summary

				\$ Change 2005 to 2004	% Change 2005 to 2004
Operating	2005	2004	2003		
Water sales	\$ 4,052,394	\$ 3,254,251	\$ 2,456,519	\$ 798,143	24.5 %
Connection fees	483,745	237,675	92,536	246,070	103.5
Service	10,479	13,540	35,202	(3,061)	(22.6)
Other	188,743	128,214	36,760	60,529	47.2
Total operating	4,735,361	3,633,680	2,621,017	1,101,681	30.3
Non-operating					
State grants	11,667	259,667	-	(248,000)	(95.5)
Interest income	457,382	405,201	209,395	52,181	12.9
Impact fees	704,709	1,054,174	1,604,418	(349,465)	(33.2)
SID assessments	5,182,900	2,546,878	669,408	2,636,022	103.5
Gain on sale of fixed assets	169,846	-	-	169,846	-
Other non-operating revenue	115,896	-	-	115,896	-
Total non-operating	6,642,400	4,265,920	2,483,221	2,376,480	55.7
Total revenue	\$ 11,377,761	\$ 7,899,600	\$ 5,104,238	\$ 3,478,161	44.0 %

Net of the increase in SID assessment collections, total District revenue increased 15.7% compared to a 3.5% increase in District expenses, excluding non-cash depreciation expense.

Including SID assessment collections, non-operating revenue increased 55.7% in 2005. Promontory SID assessment collections increased by \$2.6 million or 103.5% over 2004. In 2005, the District collected 278 Promontory SID assessments, nearly triple the amount anticipated by the developer. SID assessment collections were lower in 2003 because they were only collected for five months during that year and a brief lull in the building boom was experienced that summer.

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Impact fee revenue declined 33.2% in 2005, although this is not a result of slower development within the District. In 2004, most lot owners in The Colony, including the developer, prepaid their impact fees so fewer impact fees will be collected from them in the future. Also, the majority of growth within the District is in the Promontory development, which has lower impact fees than other service areas in the District due to the creation of the Promontory SID to fund most of the infrastructure within that development. Most of the 2005 impact fee collections were used to make debt service payments on the District's \$33.0 million revenue bonds.

The higher impact fee collections reported in 2003 actually covers three years of collections. Collections in 2001 and 2002 could not be recognized as revenue until 2003 when the District's impact fee resolution was adopted. Prior to that time, developers and lot owners building homes were required to pay an impact fee deposit and sign a deposit agreement indicating that their deposit would be converted to an impact fee once the District's resolution was adopted.

The higher impact fee collections in 2004 and previous years were placed in an escrow account, as required by state law, with a December 31, 2005 balance of almost \$2.0 million. These funds will be used to retire debt in future years as impact fee collections fluctuate with the construction cycle and current developments build out. Because of impact fee pre-payments by Colony lot owners and the lower impact fee for the Promontory development, cash impact fee collections could decline over time.

The District also sold land for \$464,846 in 2005. The District purchased the land for \$295,000, thus realizing a gain on this sale of \$169,846. In addition, the District received a one-time payment of \$100,000 from a developer.

Summary of Expenses

Excluding non-cash depreciation expense, overall expenses increased 3.5% in 2005, compared to a 15.7% increase in overall revenue excluding SID assessments that are used exclusively to retire the related SID bonds.

Including non-cash depreciation expense, the District experienced a 10.1% increase in overall expenses in 2005, or \$537,858. This is about one-fifth of the overall percentage increase in revenue, although the increase in revenue was driven largely by additional SID assessment collections. Depreciation expense increased significantly in 2005 as the Lost Canyon water importation project was completed.

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District capital projects are not expensed when constructed. Instead, their cost is amortized over their useful lives, typically 25 to 60 years. This way their cost can be matched with the revenue generated from operating the capital facilities over their useful lives. The District completed the Lost Canyon project in early 2005 leading to the increase in depreciation expense over 2004, although the increase was less than expected because the project took several more months to complete than anticipated.

Water production costs such as power, treatment, and water lease fees increased in 2005 as well due to water usage by new customers and because the new treatment plant started operations. Operations, maintenance, and repairs costs increased for the same reason. Administrative costs including management and finance, and legal services declined in 2005. The District significantly reduced its legal fees in 2005 by utilizing Summit County staff attorneys whose hourly rates are much lower than private attorneys.

It should be noted that the District has capitalized interest expense, as required, over the past few years as it implemented its aggressive capital project plan to resolve the water shortage and quality problems within its service areas. Accounting standards require interest expense to be capitalized (i.e. included in construction costs) until the projects funded by the related debt proceeds are complete. With these projects now complete, the District will capitalize little or no interest expense in the next few years. For 2005, the District capitalized \$383,603 in interest expense. Thus, interest expense will increase in 2006 even though no new debt is expected to be issued and actual cash interest payments will decline.

Mountain Regional Water Special Service District's Expense Summary

	2005	2004	2003	\$ Change 2005 to 2004	% Change 2005 to 2004
Operating					
Water production	\$ 747,972	\$ 626,970	\$ 564,845	\$ 121,002	19.3 %
Engineering and water development	94,037	64,063	159,190	29,974	46.8
Operations, maintenance and repairs	1,069,234	965,432	914,006	103,802	10.8
Management and finance	284,423	288,476	341,838	(4,053)	(1.4)
Legal services	86,019	152,864	184,998	(66,845)	(43.7)
Depreciation	1,053,157	679,372	615,816	373,785	55.0
Total operating	3,334,842	2,777,177	2,780,693	557,665	20.1
Non-Operating					
Interest expense	2,399,724	2,374,322	1,788,368	25,402	1.1
Trustee and bank fees	35,664	25,180	29,242	10,484	41.6
Bond issuance cost amortization	107,882	163,575	138,497	(55,693)	(34.0)
Total non-operating	2,543,270	2,563,077	1,956,107	(19,807)	(0.8)
Total expenses	\$ 5,878,112	\$ 5,340,254	\$ 4,736,800	\$ 537,858	10.1 %

From 2003 to 2006, the operating expense per Equivalent Residential Connection is projected to increase by 7.7%. Over the past four years, inflation according to the Consumer Price Index has increase by 12.1%. This demonstrates efficiencies and economies of scale for District operations.

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Budgetary Information

The District had favorable budget variances in 2005 for both total operating revenue and expenses, as well as for total non-operating revenues and expenses. This is true for both the 2005 Initial Budget adopted in December 2004; and the 2005 Amended Budget prepared in September 2005 and adopted in December 2005. The 2005 Amended Budget incorporated only two changes. First, \$40,000 was transferred from contingency to operations, maintenance, and repairs to hire an operator for the new water treatment plant. Second, \$20,000 in savings from the legal services budget was transferred to engineering and water development to cover anticipated professional SCADA / telemetry services. All other budget line items were unchanged.

Mountain Regional Water Special Service District's Budget Comparison

	2005 Actual	2005 Initial Budget	Favorable (Unfavorable)	2005 Amended Budget	Favorable (Unfavorable)
Operating revenues:					
Water sales	\$ 4,052,394	\$ 3,650,000	\$ 402,394	\$ 3,650,000	\$ 402,394
Connection fees	483,745	166,000	317,745	166,000	317,745
Service	10,479	11,600	(1,121)	11,600	(1,121)
Other	188,743	45,100	143,643	45,100	143,643
Total operating revenue	4,735,361	3,872,700	862,661	3,872,700	862,661
Operating Expenses:					
Water production	747,972	765,700	17,728	765,700	17,728
Engineering and water development	94,037	95,400	1,363	115,400	21,363
Operations, maintenance and repairs	1,069,234	1,039,900	(29,334)	1,079,900	10,666
Management and finance	284,423	327,200	42,777	327,200	42,777
Legal services	86,019	184,000	97,981	164,000	77,981
Depreciation	1,053,157	1,239,000	185,843	1,239,000	185,843
Total operating expenses	3,334,842	3,651,200	316,358	3,691,200	356,358
Operating income	1,400,519	221,500	1,179,019	181,500	1,219,019
Non-operating revenues (expenses)					
State grants	11,667	25,000	(13,333)	25,000	(13,333)
Interest income	457,382	221,900	235,482	221,900	235,482
Impact fees	704,709	600,000	104,709	600,000	104,709
SID assessments	5,182,900	2,437,000	2,745,900	2,437,000	2,745,900
Gain on sale of fixed assets	169,846	-	169,846	-	169,846
Other non-operating revenue	115,896	-	115,896	-	115,896
Interest expense	(2,399,724)	(2,810,900)	411,176	(2,810,900)	411,176
Trustee and bank fees	(35,664)	(32,700)	(2,964)	(32,700)	(2,964)
Bond issuance cost amortization	(107,882)	(107,900)	18	(107,900)	18
Total non-operating revenues	4,099,130	332,400	3,766,730	332,400	3,766,730
Income before operating transfers	5,499,649	553,900	4,945,749	513,900	4,985,749
Contingency	-	50,000	(50,000)	10,000	(10,000)
Net change in equity	\$ 5,499,649	\$ 503,900	\$ 4,995,749	\$ 503,900	\$ 4,995,749

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The most notable positive budget variance, which resulted in a significant portion of net income for the District in 2005, is the strong Promontory lots sales and the related SID assessment collections that more than double what was anticipated. These revenue collections can only be used to pay off the SID bonds. Other significant positive variances resulted from regulatory delays on the Lost Canyon importation project, including lower depreciation expense because the project was depreciated for only part of 2005, higher interest earnings on construction funds that were invested over a longer period of time, and lower interest expense due to the capitalization of bond interest expense.

In addition, operating revenue significantly surpassed budget projections. This resulted from the accelerating building boom, including the construction of 243 new homes, the addition of nearly 500 platted lots, and the construction of a new golf course at the Promontory years sooner than expected.

In response to this rapid growth in operating revenue, the District lowered the standby fee charged to undeveloped lots from \$38.50 per month to \$33.50 per month in 2006. In May 2006, the District reduced the rate charged to condominium homeowner's associations for water used to water each unit's front and back yards in order to make this rate more comparable to an equal number of residential water users consuming outdoor water. The lower rate does not apply to amenities provided by condominium homeowner's associations such as lakes, waterfalls, parks, trails, swimming pools, common space, etc.

Capital Assets

The District operates as an enterprise fund, which includes the capitalization and depreciation of all assets. Asset categories include land and water rights; infrastructure not buildings (water system infrastructure); construction in progress; and buildings, equipment and furnishings.

As shown below, the District's capital assets (net of depreciation) as of December 31, 2005 amounted to \$48.0 million – an increase of \$618,612 or just 1.3% over 2004 as the District's aggressive capital projects plan to address the water shortages and quality problems within the District's service areas was completed in early 2005. Because the amounts shown below are net of depreciation, the amount of cash expended for capital projects as shown in other areas of these financial statements may be different.

The District had close to \$19.5 million in construction in progress on December 31, 2004 for projects that were completed in early 2005. Thus, construction in progress was zero on December 31, 2005 while the other fixed asset categories shown below had corresponding increases between 2004 and 2005.

**Mountain Regional Water
Special Service District
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Management's Discussion and Analysis
December 31, 2005**

**Mountain Regional Water Special Service District's Capital Assets
(net of depreciation)**

	2005	2004	2003	\$ Change 2005 to 2004	% Change 2005 to 2004
Land and water rights	\$ 14,746,703	\$ 14,523,941	\$ 14,523,941	\$ 222,762	1.5 %
Infrastructure not buildings	29,030,061	12,334,029	12,024,611	16,696,032	135.4
Construction in progress	-	19,473,804	7,801,636	(19,473,804)	(100.0)
Buildings, equipment and furnishings	4,222,982	1,049,360	1,086,893	3,173,622	302.4
Total capital assets (net)	<u>\$ 47,999,746</u>	<u>\$ 47,381,134</u>	<u>\$ 35,437,081</u>	<u>\$ 618,612</u>	<u>1.3 %</u>

Between 2003 and 2004 capital assets net of depreciation increased by over \$11.9 million largely due to construction on the Lost Canyon water importation project.

The District is currently working with Park City and Weber Basin Water Conservancy District to expand the capacity of the Lost Canyon project to meet the water needs for future growth in the Snyderville Basin. Weber Basin has committed to pay the construction costs for this expansion, net of any federal grants it receives.

Outstanding Debt

The District maintains a schedule to pay off all its bonds by 2033. The District's debt level resulted from the need to acquire additional water rights, sources, and infrastructure to provide water to struggling service areas acquired or annexed into the District that were experiencing water shortages and quality problems.

Mountain Regional Water Special Service District's Outstanding Debt

	2005	2004	2003	\$ Change 2005 to 2004	% Change 2005 to 2004
Revenue and refunding bonds	\$ 32,900,000	\$ 32,900,000	\$ 33,000,000	\$ -	- %
Temporary bond anticipation note	\$ -	\$ -	\$ 28,750,000	-	-
Special assessment bonds	16,000,000	17,300,000	18,637,000	(1,300,000)	(7.5)
State notes and bonds	1,022,526	1,131,926	1,241,326	(109,400)	(9.7)
Capital lease	-	9,546	23,086	(9,546)	(100.0)
Total debt outstanding	<u>\$ 49,922,526</u>	<u>\$ 51,341,472</u>	<u>\$ 81,651,412</u>	<u>\$ (1,418,946)</u>	<u>(2.8) %</u>

The District issued no new debt in 2005. Its efforts to develop new infrastructure and acquire additional water rights to address the water shortages and quality problems within many of its acquired or annexed service areas has been largely accomplished. Total debt outstanding declined in 2005 because the District made principal payments of more than \$1.4 million.

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The debt level shown for 2003 is an anomaly. In December 2003, the District issued \$33.0 million in permanent revenue bonds that were used to pay off a temporary bond anticipation note of \$28.75 million. The temporary note was not paid off until March 2004 in order to reduce the prepayment penalty. The District issued the permanent bonds earlier than needed to take advantage of historically low interest rates.

As shown above, the District has several low and no interest notes and bonds financed through the State of Utah with a total outstanding principal balance of just over \$1.0 million. The District's capital lease for heavy equipment was paid in full in 2005.

The District paid \$1.3 million in principal on \$18.6 million Promontory SID bond in 2005, leaving an outstanding principal balance of \$16.0 million. Currently, the District has \$6.6 million set aside in debt reserves for this bond. Starting in 2008, the District can start retiring outstanding bonds ahead of schedule per the related bond covenants.

Although no principal was paid on the \$33.0 million revenue and refunding bonds in 2005, slowly increasing principal payments begin in 2006. The District's current revenue sources are sufficient to pay all bond payments into the foreseeable future.

The District annexed Timberline Service District's water system in 2005. This small district added approximately 120 new customers, having only a minimal effect on operating revenue and expense. In early 2006, the District will assume a zero interest state loan from Timberline in the amount of \$278,000. Annual principal payments will be made through 2018 in amounts of \$21,000 to \$22,000. The additional revenue received by the District from the new Timberline customers less the related increase in new expense exceed the annual principal payment, resulting in a small net increase in cash flow for the District.

The District is required by several bond covenants to maintain a debt service coverage ratio of at least 1.25 times. For 2005, this ratio was 1.97. This ratio should be less in 2006 because principal payments begin again on the \$33.0 million revenue and refunding bonds, plus the District implemented small rate reductions for 2006. Further, a potential increase in electrical rates could be approved by the Utah Public Service Commission in the fall of 2006.

The District's most recent underlying ratings by Fitch and Standards & Poor is "BBB". The District's \$33,000,000 Revenue and Refunding Bonds – Series 2003 were insured at an "AAA" rating.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Management's Discussion and Analysis
December 31, 2005**

Requests for Information

This financial report is designed to provide a general overview of Mountain Regional Water Special Service District's finances for all those interested. Questions concerning this or other financial information should be addressed to the Chief Financial Officer, Mountain Regional Water Special Service District, 6421 N. Business Park Loop Road – Suite A, P.O. Box 982320, Park City, Utah 84098.

Basic Financial Statements

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Balance Sheets
December 31, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
<u>ASSETS</u>		
Current assets:		
Cash	\$ 1,132,515	\$ 501,656
Restricted cash	7,161,249	5,048,605
Accounts receivable	507,610	479,873
Other receivables	4,504	19,035
Prepaid expenses	257,324	257,721
Inventory	43,408	41,150
Total current assets	9,106,610	6,348,040
Cash restricted for debt repayment	6,100,759	5,687,628
Capital assets:		
Depreciable assets, net	33,253,043	13,383,388
Land and water rights	14,746,703	14,523,941
Construction-in-progress	-	19,473,805
Other assets, net	1,314,892	1,397,188
	<u>\$ 64,522,007</u>	<u>\$ 60,813,990</u>

See accompanying notes and independent auditors' report.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Balance Sheets, Continued
December 31, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
<u>LIABILITIES</u>		
Current liabilities:		
Accounts payable	\$ 58,260	\$ 309,098
Accrued liabilities	620,010	563,158
Due to other government entities	168,405	345,655
Current portion of long-term debt	1,510,400	1,409,400
Accrued liability - impact fees	27,333	-
Current portion, accrued liability - developer	14,132	-
Current portion, obligations under capital lease	-	9,546
Total current liabilities	<u>2,398,540</u>	<u>2,636,857</u>
Accrued liability - developer, less current portion	2,100,632	2,143,547
Long-term debt, net of current portion	<u>48,412,126</u>	<u>49,922,526</u>
Total liabilities	<u>52,911,298</u>	<u>54,702,930</u>
<u>NET ASSETS</u>		
Invested in capital assets, net of related debt	7,198,771	3,631,451
Restricted	1,802,768	859,252
Unrestricted	<u>2,609,170</u>	<u>1,620,357</u>
Fund equity	<u>11,610,709</u>	<u>6,111,060</u>
	<u>\$ 64,522,007</u>	<u>\$ 60,813,990</u>

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Statements of Revenues, Expenses
and Changes in Net Assets
Years Ended December 31, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
Operating revenues:		
Water sales	\$ 4,052,394	\$ 3,254,251
Connection fees	483,745	237,675
Service	10,479	13,540
Other	188,743	128,214
Total operating revenues	<u>4,735,361</u>	<u>3,633,680</u>
Operating expenses:		
Water production	747,972	626,970
Engineering and water development	94,037	64,063
Operations, maintenance and repairs	1,069,234	965,432
Management and finance	284,423	288,476
Legal services	86,019	152,864
Depreciation	1,053,157	679,372
Total operating expenses	<u>3,334,842</u>	<u>2,777,177</u>
Operating income	<u>1,400,519</u>	<u>856,503</u>
Non-operating revenues (expenses):		
State grants	11,667	259,667
Interest income	457,382	405,201
Impact fees	704,709	1,054,174
SID assessments	5,182,900	2,546,878
Gain on sale of land	169,846	-
Other non-operating revenue	115,896	-
Interest expense	(2,399,724)	(2,374,322)
Trustee and bank fees	(35,664)	(25,180)
Bond issuance cost amortization	(107,882)	(163,575)
Total non-operating revenues	<u>4,099,130</u>	<u>1,702,843</u>
Income before transfers	<u>5,499,649</u>	<u>2,559,346</u>
Net income	<u>5,499,649</u>	<u>2,559,346</u>
Net assets, beginning of year	<u>6,111,060</u>	<u>3,551,714</u>
Net assets, end of year	<u>\$ 11,610,709</u>	<u>\$ 6,111,060</u>

See accompanying notes and independent auditors' report.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Statements of Cash Flows
Years Ended December 31, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Cash received from customers	\$ 4,722,155	\$ 3,616,654
Cash paid to employees and suppliers	<u>(2,654,782)</u>	<u>(2,006,567)</u>
Net cash from operating activities	<u>2,067,373</u>	<u>1,610,087</u>
Cash flows from non-capital financing activities:	<u>-</u>	<u>-</u>
Cash flows from capital and related financing activities:		
Purchase of property and equipment,	(1,583,165)	(11,858,695)
Proceeds from state capital grant	-	259,667
Interest paid	(2,832,911)	(3,164,153)
Lease payments	(9,546)	(13,540)
Long-term debt payments	(1,409,400)	(30,296,400)
Capitalized bond issuance costs	-	(297,100)
Net repayments of pre-paid impact fees	27,333	(676,947)
Payments on accrued liability - developer	(28,783)	(1,838,381)
SID assessment	5,182,900	2,546,878
Impact fees	704,709	1,054,174
Proceeds from sale of land	464,846	-
Other revenue received	<u>115,896</u>	<u>-</u>
Net cash from capital and related financing activities	<u>631,879</u>	<u>(44,284,497)</u>
Cash flows from investing activities:		
Interest received	<u>457,382</u>	<u>405,201</u>
Net change in cash	3,156,634	(42,269,209)
Cash - beginning of period	<u>11,237,889</u>	<u>53,507,098</u>
Cash - end of period	<u><u>\$ 14,394,523</u></u>	<u><u>\$ 11,237,889</u></u>
Cash reported on the balance sheet:		
Cash	\$ 1,132,515	\$ 501,656
Restricted cash	7,161,249	5,048,605
Cash restricted for debt repayment	<u>6,100,759</u>	<u>5,687,628</u>
	<u><u>\$ 14,394,523</u></u>	<u><u>\$ 11,237,889</u></u>

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Statements of Cash Flows, Continued
Years Ended December 31, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
Reconciliation of net loss to net cash from operating activities:		
Net operating income	\$ 1,400,519	\$ 856,503
Adjustments to reconcile net operating income (loss) to net cash from operating activities:		
Depreciation	1,053,157	679,372
Changes in operating assets and liabilities:		
Accounts receivable	(27,737)	(170,937)
Other receivables	14,531	153,911
Prepaid expenses	397	104,063
Inventory	(2,258)	21,396
Accounts payable	(250,838)	(472,069)
Accrued liabilities	56,852	164,425
Due to other government entities	(177,250)	273,423
Total adjustments	<u>666,854</u>	<u>753,584</u>
Net cash from operating activities	<u>\$ 2,067,373</u>	<u>\$ 1,610,087</u>

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements
December 31, 2005 and 2004**

(1) Summary of Significant Accounting Policies

This summary of significant accounting policies of Mountain Regional Water Special Service District (the District) is presented to assist in understanding the District's financial statements. The financial statements and notes are representations of the District's management, who are responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles, and have been consistently applied in the preparation of these financial statements.

Operations

The District was formed in 1987 pursuant to a resolution passed and adopted by the Summit County Board of Commissioners providing for the creation of the Atkinson Special Service District of Summit County, Utah. On January 1, 2000 the name was changed to Mountain Regional Water Special Service District. The District was created to provide improved water utility services to an area of new growth and development within the Snyderville Basin and Promontory Development of Summit County.

Reporting Entity

The District is a component unit of Summit County, Utah and, as such, has been included in the basic financial statements of Summit County, Utah. The District is governed by the Summit County Board of Commissioners.

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**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(1) Summary of Significant Accounting Policies, Continued

Accounting Policies

The District operates as an enterprise fund. Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the costs (expenses, including depreciation) of providing services to the public on a continuing basis are financed through user charges. Revenue from water sales is recorded based on monthly usage at stated rates. Other revenues are recorded when services are performed.

Effective January 1, 2003, the District adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Government*. GASB Statement No. 37, *Basic Financial Statements and Management’s Discussion and Analysis – for State and Local Governments: Omnibus*, and GASB Statement No. 38, *Certain Financial Statement Disclosures*. The District follows all Governmental Accounting Standards Board (GASB) pronouncements as well as the Financial Accounting Standards Board pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Budgetary Policy

Budgetary procedures for the District have been established by Utah State Statute in Title 17A – Special Districts. The District uses the same accounting method for preparing the budget as is used for financial reporting.

Annual proprietary fund operating and capital budgets are prepared in accordance with state law. On or before the first regularly scheduled meeting of the Summit County Commission in November, the Commission must adopt a tentative budget for the following fiscal year for public review. At least thirty days after the tentative budget is adopted, but no later than December 31, the Commission must hold a public hearing on the tentative budget. A final budget must be adopted by the Commission no later than December 31.

Budgets may be increased by resolution of the Commission at any time during the fiscal year at a regular meeting or special meeting called for that purpose. Summit County policy requires that any such meeting must be publicly noticed for at least two weeks.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(1) Summary of Significant Accounting Policies, Continued

Budgetary Policy, Continued

Under Utah Code, the District's budget establishes maximum legal authorization for expenses during the fiscal year. Expenses are not to exceed budgeted amounts, including revisions, except as allowed by the code for certain events.

Cash Equivalents

The District considers all highly liquid debt instruments with a maturity of three months or less when purchased to be cash equivalents.

Accounts Receivable

The District considers all accounts receivable to be collectible.

Inventory

Inventories are recorded at the lower of cost or market on a first-in, first-out basis.

Depreciation and Amortization

The costs of property and equipment are depreciated using the straight-line method over estimated useful lives ranging from 5 to 60 years.

Capitalized Interest Expense

The District capitalizes interest in connection with the construction of water systems financed through debt. Interest capitalization ceases when water systems are completed and available for use. For the years ended December 31, 2005 and 2004, the District incurred gross interest expense of \$2,832,911 and \$3,164,153, of which \$383,603 and \$764,730, respectively, was capitalized.

Comprehensive Income

Comprehensive income approximates net income for the years ended December 31, 2005 and 2004.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(1) Summary of Significant Accounting Policies, Continued

Estimations and Assumptions

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(2) Deposits and Investments

Deposits and investments for the District are governed by the Utah Money Management Act (*Utah Code Annotated*, Title 51, Chapter 7, "the Act") and by the rules of the Utah Money Management Council ("the Council"). Following are discussions of risks related to its cash management activities.

Custodial Credit Risk

Deposits. Custodial credit risk for deposits is the risk that in the event of a bank failure, the District's deposits may not be recovered. The District's policy for managing custodial credit risk is to adhere to the Money Management Act. The Act requires all deposits of the District to be in a *qualified depository*, defined as any financial institution whose deposits are insured by an agency of the federal government and which has been certified by the Commissioner of Financial Institutions as meeting the requirements of the Act and adhering to the rules of the Utah Money Management Council.

As of December 31, 2005, \$932,515 of the District's bank balance of \$1,132,515 was uninsured and uncollateralized. As of December 31, 2004, \$301,565 of the District's bank balance of \$501,565 was uninsured and uncollateralized.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(2) Deposits and Investments, Continued

Credit Risk

Investments. Credit risk is the risk that the counterparty to an investment will not fulfill its obligations. The District's policy for limiting the credit risk is to comply with the Utah Money Management Act.

The District is authorized to invest in the Utah Public Treasurer's Investment Fund (PTIF), an external pooled investment fund managed by the Utah State Treasurer subject to the Act and Council requirements. The PTIF is not registered with the SEC as an investment company, and deposits in the PTIF are not insured or otherwise guaranteed by the State of Utah. The PTIF operates and reports to participants on an amortized basis. The income, gains, and losses, net of administrative fees, of the PTIF are allocated based upon the participant's average daily balances.

As of December 31, 2005 and 2004, the District had \$4,491,471 and \$2,631,589, respectively, invested directly with the PTIF. In addition, the District had as of December 31, 2005 and 2004 respectively, \$6,850,102 and \$5,311,102 of debt service reserve, bond sinking fund, and bond proceeds invested with the PTIF through Wells Fargo Corporate Trust, who acts as trustee for these funds. The amounts invested with the PTIF are reported at fair value. The entire balance had a maturity of less than one year. The PTIF pool has not been rated.

As of December 31, 2005 and 2004 respectively, the District had \$2,955,003 and \$2,958,304 invested in a guaranteed investment contract with Bank of America. The funds invested represent the debt service reserve for Series 2003 \$33 million revenue and refunding bond. Bank of America is required to invest the funds in accordance with the Utah Money Management Act. Wells Fargo Corporate Trust acts as trustee for this investment.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The local government manages its exposure to declines in fair value by investing mainly in the PTIF and by adhering to the Utah Money Management Act. The Act requires that the remaining term to maturity of the investment may not exceed the period of availability of the funds to be invested.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(3) Capital Assets

Capital asset activity for the year ending December 31, 2005 was as follows:

	Balance January 1, 2005	Additions	Dispositions / Transfers	Balance December 31, 2005
Capital assets not being depreciated:				
Land and water rights	\$ 14,523,941	\$ 516,656	\$ (293,893)	\$ 14,746,703
Construction-in-progress	19,473,804	1,282,506	(20,756,310)	-
	<u>33,997,745</u>	<u>1,799,162</u>	<u>(21,050,203)</u>	<u>14,746,703</u>
Depreciable assets:				
Buildings	535,390	3,043,540	-	3,578,930
Improvements other than buildings	15,957,788	17,521,238	-	33,479,026
Furniture and fixtures	147,387	18,279	-	165,666
Machinery and equipment	551,432	220,398	-	771,830
Vehicles	122,461	119,356	-	241,817
Engineering library	108,675	-	-	108,675
	<u>17,423,133</u>	<u>20,922,811</u>	<u>-</u>	<u>38,345,944</u>
Accumulated depreciation	<u>(4,039,744)</u>	<u>(1,053,157)</u>	<u>-</u>	<u>(5,092,901)</u>
	<u>13,383,389</u>	<u>19,869,654</u>	<u>-</u>	<u>33,253,043</u>
	<u>\$ 47,381,134</u>	<u>\$ 21,668,816</u>	<u>\$ (21,050,203)</u>	<u>\$ 47,999,746</u>

Depreciation expense for 2005 and 2004 was \$1,053,157 and \$679,372, respectively.

(4) Other Assets

As of December 31, 2005 and 2004, other assets were made up of capitalized debt issuance costs of \$1,862,133 and \$1,836,546 net of accumulated amortization of \$547,241 and \$439,358, respectively. The debt issuance costs are being amortized over the life of the related debts (up to thirty years).

(5) Accrued Liabilities

Accrued liabilities consist of accrued wages and benefits, customer deposits, pre-paid water reservation fees and interest on outstanding debt.

**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(6) Long-Term Debt

A summary of long-term debt activity for the year ended December 31, 2005 is as follows:

	<u>Balance January 1, 2005</u>	<u>New Debt Issued or Acquired</u>	<u>Principal Payments</u>	<u>Balance December 31, 2005</u>	<u>Due Within One Year</u>
Notes payable	\$ 229,926	\$ -	\$ 40,400	\$ 189,526	\$ 40,400
Bonds payable	51,102,000	-	1,369,000	49,733,000	1,470,000
	<u>\$ 51,331,926</u>	<u>\$ -</u>	<u>\$ 1,409,400</u>	<u>\$ 49,922,526</u>	<u>\$ 1,510,400</u>

The District has two outstanding notes payable to the State of Utah, Department of Natural Resources – Division of Water Resources. The notes were assumed as part of acquisitions of water companies by the District. The notes are secured by property and require annual payments.

The District's bonds consist of water revenue and special assessment bonds. Water revenue bonds are secured by the revenues of the District. Special assessment bonds are secured by special assessments of special improvement districts. Principal and interest payments are due annually and semi-annually.

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**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(6) Long-Term Debt, Continued

The District has issued the following notes and bonds payable as of December 31, 2005 and 2004:

Series	Original Issue	Interest Rate	Maturity Date	Principal Outstanding	
				2005	2004
Notes Payable					
State of Utah, Dept. of Natural Resources - Div. of Water Resources					
Note	\$ 258,000	None	2007	\$ 54,732	\$ 82,032
Note	324,000	None	2016	134,794	147,894
				<u>189,526</u>	<u>229,926</u>
Bonds Payable					
Water revenue					
1991	295,000	5.00%	2012	164,000	180,000
2002	357,000	1.51%	2022	310,000	326,000
2002B	433,000	None	2015	359,000	396,000
2003	33,000,000	2.0% - 5.0%	2033	32,900,000	32,900,000
Special assessment					
2003	\$ 18,600,000	6.25% - 7.0%	2018	16,000,000	17,300,000
				<u>49,733,000</u>	<u>51,102,000</u>
				49,922,526	51,331,926
			Less current portion	<u>(1,510,400)</u>	<u>(1,409,400)</u>
				<u>\$ 48,412,126</u>	<u>\$ 49,922,526</u>

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**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(6) Long-Term Debt, Continued

As of December 31, 2005, the aggregate maturities of notes and bonds payable, including interest, are as follows:

Years Ending December 31,	Promissory Notes		Bonds Payable		Total Debt Service Requirement
	Principal	Interest	Principal	Interest	
2006	\$ 40,400	\$ -	1,470,000	\$ 2,719,096	\$ 4,229,496
2007	40,532	-	1,481,000	2,631,004	4,152,536
2008	13,100	-	1,493,000	2,542,113	4,048,213
2009	13,100	-	1,494,000	2,452,786	3,959,886
2010	13,100	-	1,405,000	2,357,109	3,775,209
2011-15	65,500	-	7,662,000	10,411,511	18,139,011
2016-20	3,794	-	7,227,000	7,931,335	15,162,129
2021-25	-	-	6,771,000	6,267,686	13,038,686
2026-30	-	-	11,205,000	4,165,750	15,370,750
2031-33	-	-	9,525,000	979,000	10,504,000
	<u>\$ 189,526</u>	<u>\$ -</u>	<u>\$ 49,733,000</u>	<u>\$ 42,457,390</u>	<u>\$ 92,379,916</u>

(7) Capital Lease

The District leases equipment under a capital lease, which expired in 2005. The cost of the equipment, \$62,710 was capitalized in the District's property and equipment. During the years 2005 and 2004, the District made payments on this lease totaling \$ 9,789 and \$14,685, respectively.

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**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(8) Accrued Liability – Developer

The District entered into an agreement with a developer during 2000 regarding the prepayment of municipal and industrial use impact fees. Under the terms of this agreement, the developer agreed to pre-pay the District \$6,300 per residential Equivalent Connection (REC) for 240 REC's. These pre-paid impact fees were recorded by the District as an accrued liability to the developer. During 2004, the developer pre-paid an additional \$1,201,612 for the irrigation impact fee or an additional \$9,129 per lot on the lots still owned by the developer. The developer also pre-paid the total impact fee for two other lots at \$16,650 each. These pre-paid impact fees were recorded by the District as an accrued liability to the developer.

The District is to repay this liability to the developer through the collection of impact fees from individuals who purchase the building lots from the developer. The outstanding accrued liability to this developer for pre-paid impact fees as of December 31, 2005 and 2004 was \$1,542,632 and \$1,557,283, respectively.

During 2002, the District established Special Improvement District No. 2002-1 and in 2003 issued the Special Assessment Bonds Series 2003 (the SID bonds). In accordance with the terms of the bonds, the developer deposited \$558,000 into a bond stabilization fund with the District to be used for bond repayment in the event of default by the developer. When the SID bonds are fully retired, the District will refund the deposit to the developer if no event of default has occurred. Accordingly, the deposit is recorded as an accrued liability to the developer as of both December 31, 2005 and 2004.

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**Mountain Regional Water
Special Service District
A Component Unit of Summit County, Utah
Notes to Financial Statements, Continued
Years Ended December 31, 2005 and 2004**

(9) Related Party Transactions

The District, from time to time, enters into agreements with Summit County, a related party. Historically, these agreements have included the leasing of certain vehicles, the payment of water reservation and lease fees on behalf of the District, loans for working capital, and the shared services of an employee. As of December 31, 2005 and 2004, the amount payable to Summit County was \$168,405 and \$345,655, respectively.

(10) Contingency

Predecessor water companies and services districts that annexed into the District entered into agreements to provide future connections without assessing an impact fee in exchange for water rights, sources, and other infrastructure. As a result, the District may incur a reduction in future impact fee collections.

(11) Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by commercial insurance purchased from independent third parties. The District is a member of the Utah Local Governments Trust (ULGT), a public entity risk pool currently operating as a common risk management and insurance program for Utah State governments. The District pays an annual premium to ULGT for its general insurance coverage. During 2005, the District did not increase any level of insurance coverage. Settlement amounts have not exceeded insurance coverage for the current year or the prior years.

(12) Subsequent Event

In early 2006, the District assumed a zero interest state loan from Timberline Service District, which was annexed by the District in 2005, in the amount of \$278,000. Annual principal payments will be made through 2018 in amounts of \$21,000 to \$22,000.

**MOUNTAIN REGIONAL WATER
SPECIAL SERVICE DISTRICT
A COMPONENT UNIT OF SUMMIT COUNTY
Government Auditing Standards and
State of Utah Legal Compliance
Year Ended December 31, 2005**

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

**The Governing Board
Mountain Regional Water Special Service District**

We have audited the basic financial statements of Mountain Regional Water Special Service District (the District), a component unit of Summit County, Utah, as of and for the year ended December 31, 2005, and have issued our report thereon dated April 28, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Mountain Regional Water Special Service District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be a material weakness. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operations that we consider to be material weaknesses.

Compliance

As part of obtaining reasonable assurance about whether Mountain Regional Water Special Service District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement accounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

However, we noted certain matters that we reported to management of Mountain Regional Water Special Service District in a separate letter dated April 28, 2006.

This report is intended solely for the information and use of the audit committee, management, others within the organization, and the County Commission and is not intended to be and should not be used by anyone other than these specified parties.

Schmize, Luffites, Inniss; C..P.C.

April 28, 2006

INDEPENDENT AUDITORS' REPORT ON THE STATE OF UTAH LEGAL COMPLIANCE

The Governing Board Mountain Regional Water Special Service District

We have audited the basic financial statements of Mountain Regional Water Special Service District (the District), a component unit of Summit County, Utah, for the year ended December 31, 2005, and have issued our report thereon dated April 28, 2006. As part of our audit, we have audited the District's compliance requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; special tests and provisions applicable to its major State assistance program as required by the State of Utah Legal Compliance Audit Guide for the year ended December 31, 2005. The District received the following major assistance program from the State of Utah:

Conservation and Development Fund (DNR, Division of Water Resources)

The District did not receive any non-major State grants for the year ended December 31, 2005.

Our audit included test work on the District's compliance with the following general compliance requirements identified in the State of Utah Legal Compliance Audit Guide:

- Public Debt
- Cash Management
- Purchasing Requirements
- Budgetary Compliance
- Special Districts
- Other General Compliance Issues
- Impact Fees

The management of Mountain Regional Water Special Service District is responsible for the District's compliance with all compliance requirements identified above. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed an instance of noncompliance with the requirements referred to above, which are outlined in the accompanying schedule of findings and questioned costs.

We considered these instances on noncompliance in forming our opinion on compliance, which is expressed in the following paragraph.

In our opinion, except for the instance of noncompliance listed on the accompanying schedule of findings and questioned costs, Mountain Regional Water Special Service District complied, in all material respects, with the general compliance requirements identified above for the year ended December 31, 2005.

Schmitt, Gifford, Smith & Co. P.C.

April 28, 2006

Mountain Regional Water Special Service District
State of Utah Legal Compliance Schedule of Findings
Year Ended December 31, 2005

05-1 Cash Management

Condition: During the year ended December 31, 2005, the District was in violation of Utah Code Section 51-7-15 and Rule 4 of the Utah Money Management Council related to the treasurer's fidelity bond. Utah Code Section 51-7-15 and Rule 4 of the Utah Money Management Council requires the District to maintain fidelity bond coverage of at least \$209,000. The District coverage as of December 31, 2005 was \$150,000.

Recommendation: We recommend that the District obtain the proper amount of fidelity bond coverage.

Status: The recommendation has been implemented.

May 26, 2006

To the Audit Committee of the Summit County Commission
and Management of Mountain Regional Water Special
Service District

In planning and performing our audit of the financial statements of Mountain Regional Water Special Service District (the District), a component unit of Summit County, Utah for the year ended December 31, 2005, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control.

Our consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the internal control and its operation that we consider to be material weaknesses as defined above.

However, during our audit we became aware of a matter that is an opportunity for strengthening internal controls and operating efficiency. This letter summarizes our comments and suggestions regarding this matter. We previously reported on the District's internal control in our report dated April 28, 2006. This letter does not affect our report dated April 28, 2006, on the basic financial statements of the District.

May 16, 2006

**Mountain Regional Water
Special Service District
Management Letter**

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Water Loss Monitoring and Corrective Action

Condition: The District continues to experience unidentified water losses from its system at rates significantly higher than typical water loss rates of other systems. Management is aware of the magnitude of the losses in total and asserts that major leaks are repaired as they are detected. However, because of the interconnected structure of the system, it is difficult to isolate the cause of all losses. Although the principal focus of the District's efforts has been much needed construction and acquisition related activities, the District does and will incur significant costs for continued water losses.

Recommendation: We recommend that resources and effort be focused on improving the system through installation of metering equipment at key locations to monitor losses and implement corrective action when losses are identified. By implementing this recommendation the District should reduce production costs and provide additional saleable water.

Management's Response: The District has continued its efforts to reduce water loss and will continue to do so. The District has made significant progress in this area, but recognizes the need to continue its efforts. For 2006, the District budgeted for leak detection equipment and for three more meters to be placed in strategic locations to help identify leaks more quickly. In addition, the District repaired a major leak in a storage pond in May 2006. Because the storage pond is needed during summer months for peak flow for two golf courses, and because of the very short construction season in the Synderville Basin, the District fixed the pond leak as soon as it was feasible.

Fidelity Bond Insurance

Condition: During the year ended December 31, 2005, the District was in violation of Utah Code Section 51-7-15 and Rule 4 of the Utah Money Management Council related to the treasurer's fidelity bond. Utah Code Section 51-7-15 and Rule 4 of the Utah Money Management Council requires the District to maintain fidelity bond coverage of at least \$209,000. The District coverage as of December 31, 2005 was \$150,000.

Recommendation: We recommend that the District increase the amount of coverage of the fidelity bond on the Chief Financial Officer to the required level.

Management's Response: This was due to a miscommunication with the District's insurance provider. The District had the appropriate level of insurance, with two

May 16, 2006

**Mountain Regional Water
Special Service District
Management Letter**

Page 3

individuals covered for a total of \$300,000. When a new Chief Financial Officer was hired in 2003, a request was made to change the fidelity bond into his name only. It was expected by the District the bond would remain at \$300,000, but the insurance provider issued the bond for \$150,000. This problem was corrected within two days after the District became aware of the situation.

Purchasing Policies

Condition: The District has established purchasing policies, as required under the Utah Procurement Code. During the audit, it was noted that the District's purchasing policy had been violated on several occasions.

Recommendation: We recommend that the District provide the necessary training to assure that all employees are aware of the requirements of the District's purchasing policy and that this policy be followed.

Management's Response: The District agrees that additional training is needed. In addition, the District's procurement policies are being modified to better reflect the environment the District operates within.

The preceding comments recommendations are intended solely for the information and use of the audit committee, management, and others within the organization and should not be used by anyone other than these specified parties.

We have already discussed these concerns with various District personnel, and will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Very truly,

SCHMITT, GRIFFITHS, SMITH & CO., P.C.

Sherman H. Smith, CPA